[COMMITTEE PRINT]

DESCRIPTION OF BILLS

RELATING TO

TUITION CREDITS AND DEDUCTIONS

LISTED FOR A HEARING

BY THE

SUBCOMMITTEE ON TAXATION AND DEBT MANAGEMENT

OF THE

COMMITTEE ON FINANCE

ON JANUARY 18, 19, AND 20, 1978

PREPARED FOR THE USE OF THE

COMMITTEE ON FINANCE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

JANUARY 17, 1978

U.S. GOVERNMENT PRINTING OFFICE

21-296 WASHINGTON : 1978 JCS-1-78

CONTENTS

I. INTRODUCTION

The bills described in this pamphlet have been scheduled by the Subcommittee on Taxation and Debt Management of the Committee on Finance for hearings on January 18, 19, and 20, 1978. The bills relate to income tax credits or deductions on account of tuition and certain other educational expenses.

In connection with these hearings, the staff of the Joint Committee on Taxation has prepared a description of the bills, and an explanation of the present law treatment of tuition and the issues involved in providing tuition credits and deductions.

II. DESCRIPTION OF TUITION CREDIT AND DEDUCTION PROPOSALS

Seven bills providing tax credits or deductions for educational expenses have been listed for hearings: S. 96, S. 311, S. 834, S. 954, S. 1570, S. 1781, and S. 2142. These bills and the Senate floor amendment to the Social Security Financing Amendments of 1977, which provided a credit for certain educational expenses, are described below.

A. SENATE BILLS

1. S. 96—Mr. Hollings

This bill provides a tax credit for a taxpayer's expenses for education above the 12th grade at an institution of higher education or an accredited business, trade, technical, or vocational school for himself or for any other individual. The amount of the credit is 75 percent of the first $200 of eligible expenses; 25 percent of the next $300; and 10 percent of eligible expenses between $500 and $1,500. If the expenses for one individual are paid by more than one taxpayer, the credit for that individual's expenses must be prorated among the taxpayers. The credit must be reduced by one percent of the taxpayer's adjusted gross income in excess of $25,000.

Eligible expenses are tuition, fees, books, supplies, and equipment. Meals, lodging, or similar personal, living, or family expenses are not covered. Only expenses for courses toward a baccalaureate or higher degree or for courses necessary for predetermined educational, professional, or vocational objectives may be taken into account for the credit.

Eligible expenses must be reduced by any amount received as scholarships or fellowships (excluded from income under section 117), or as education and training allowances or educational assistance allowances under chapters 33 and 35 (relating to Veterans' benefits), respectively, of title 38 of the United States Code. No trade or business expense deduction under section 162 is allowed for any expense taken into account in determining this credit.

The bill applies to the 50 States, Puerto Rico, the District of Columbia, Guam, American Samoa, the Virgin Islands, and the Trust Territory of the Pacific Islands.

The bill applies to taxable years beginning on or after the date of enactment.

2. S. 311—Mr. Roth, Mr. Church, Mr. DeConcini, Mr. Dole, Mr. Domenici, Mr. Goldwater, Mr. Huddleston, Mr. Humphrey, Mr. Leahy, Mr. Magnuson, Mr. Ribicoff, Mr. Schmitt, Mr. Stafford, and Mr. Stevens

This bill allows a tax credit for higher education expenses incurred by a taxpayer for himself, his spouse, or his dependents as full time students in courses recognized for credit toward a baccalaureate degree or in courses leading toward a certificate of required course work at a vocational school. No credit is allowed for any graduate program.

The maximum credit is $250 per student for taxable years beginning in 1977; $300 per student for taxable years beginning in 1978; $400 per student for taxable years beginning in 1979, and $500 per student for taxable years beginning in 1980 and thereafter. If a student's educational expenses are paid by more than one taxpayer, the credit with respect to that student's expenses must be prorated among the taxpayers.

Eligible expenses are tuition, fees, books, supplies, and equipment, but do not include meals, lodging, or similar personal, living, or family expenses. The eligible expenses must be reduced by any amount received as scholarships or fellowships (excluded from income under section 117), or as education and training allowances or educational assistance allowances under chapters 33 and 35 (relating to Veterans' benefits), respectively, of title 38 of the U.S. Code.

No credit is allowed for an individual's educational expenses, unless the individual is a full time student at an eligible institution for four calendar months of a year. To claim a credit for a spouse's educational expenses, the taxpayer must be entitled to an exemption under section 151(b) for his spouse, or they must file a joint return for the taxable year. No trade or business expense deduction under section 162 is allowed for any expense taken into account in determining this credit.

The bill applies to educational expenses paid after June 30, 1977, in taxable years beginning after December 31, 1976, for courses of instruction commencing after June 30, 1977.

3. S. 834—Mr. Schweiker

This bill allows a taxpayer to elect a credit or deduction for tuition paid for himself, his spouse, or his dependents.

A taxpayer electing a tuition credit may claim an amount equal to 50 percent of the total tuition paid by him for himself, his spouse, or any dependent for whom he may claim a personal exemption under section 151(e). The credit is limited to a maximum of $250 for any single individual's tuition. The taxpayer may claim a credit for a spouse's tuition only if he is entitled to an exemption for his spouse under section 151(b), or they file a joint return. Credits are allowed for tuition at institutions of higher education, including graduate schools; vocational schools; secondary schools; or elementary schools. No trade or business expense deduction under section 162 may be claimed for any tuition taken into account in determining this credit.

Alternatively, a taxpayer may elect to deduct tuition expenses. The maximum tuition deduction for any single individual's tuition is $1,000. The rules for eligible students, eligible expenses, spouse's expenses, eligible educational institutions, and the disallowance of deductions under section 162, which are applicable to tuition credits, also apply to tuition deductions.

This bill applies to taxable years beginning after the date of enactment.

4. S. 954—Mr. Durkin

This bill allows an elective credit or deduction for tuition paid by a taxpayer for himself or for another individual. The maximum credit for any individual's tuition is $300. If a taxpayer elects a tuition deduction, the maximum amount deductible with respect to any individual is $1,000.

To be creditable or deductible, tuition must be paid to institutions of higher education, including graduate schools; vocational schools; secondary schools or elementary schools. No deduction is allowed as a trade or business expense under section 162 for any educational expense taken into account in determining a tuition credit or a tuition deduction.

This bill applies to taxable years beginning after the date of enactment.

5. S. 1570—Mr. Moynihan

This bill allows a refundable tuition tax credit for elementary or secondary school tuition paid by a taxpayer for his dependent children. The amount of the credit is 50 percent of tuition paid for any dependent, but is limited to a maximum of $250 per year per dependent. The credit must be reduced by 5 percent of the taxpayer's adjusted gross income in excess of $18,000.

Expenses eligible for the credit are tuition and fees required for enrollment or attendance at a tax-exempt elementary or secondary school, but do not include meals, lodging, or similar personal, living, or family expenses.

The bill applies to taxable years beginning after the date of enactment.

6. S. 1781—Mr. Anderson

This bill allows an elective credit or deduction for tuition paid by a taxpayer to institutions of higher education (except graduate schools), vocational schools, secondary schools, or elementary schools for himself, for his spouse, or for his dependents.

The maximum credit which a taxpayer may claim for the educational expenses of any individual is $250 for taxable years beginning in 1977, $300 for taxable years beginning in 1978, $400 for taxable years beginning in 1979, and $500 for taxable years beginning in 1980 and thereafter. If more than one taxpayer pays the educational expenses of an individual, the credit with respect to that individual must be prorated among these taxpayers.

Taxpayers may elect a tuition deduction instead of a credit. The maximum deduction with respect to the expenses of any individual is $500 for taxable years beginning in 1977, $600 for taxable years beginning in 1978, $800 for taxable years beginning in 1979, and $1,000 for taxable years beginning in 1980 and thereafter. If more than one taxpayer pays the educational expenses of an individual, the deduction with respect to that individual must be prorated among such taxpayer.

For purposes of both the credit and the deduction, educational expenses of a taxpayer's spouse may be claimed only if the taxpayer is entitled to an exemption for his spouse under section 151(b) or if they file a joint return. The credit or deduction is allowed only with respect to full-time students. The expenses taken into account for determining either a credit or deduction must be reduced by scholarship or fellowship grants excluded from income under section 117, and educational assistance allowances and educational and training allowances received under chapters 35 and 33 (relating to Veterans' benefits), respectively, of title 38 of the United States Code. Expenses eligible for a credit or deduction are tuition, fees, books, supplies, and equipment, but do not include meals, lodging, or similar personal, living, or family expenses. Higher education expenses must be for courses allowed as credit toward a baccalaureate degree. Vocational school expenses must be for courses allowed as credit for a certificate of required course work.

No trade or business expense deduction under section 162 is allowed for expenses taken into account in determining any tuition credit or tuition deduction.

This bill applies to educational expenses paid after June 30, 1977, in taxable years beginning after December 31, 1976, for courses of instruction commencing after June 30, 1977.

7. S. 2142—Mr. Packwood, Mr. Moynihan, Mr. Allen, Mr. Anderson, Mr. Bentsen, Mr. Cannon, Mr. Curtis, Mr. Danforth, Mr. DeConcini, Mr. Dole, Mr. Domenici, Mr. Durkin, Mr. Garn, Mr. Goldwater, Mr. Gravel, Mr. Griffin, Mr. Hansen, Mr. Hatch, Mr. Hathaway, Mr. Hayakawa, Mr. Heinz, Mr. Helms, Mr. Humphrey, Mr. Johnston, Mr. Laxalt, Mr. Leahy, Mr. Lugar, Mr. Mathias, Mr. McClure, Mr. Melcher, Mr. Nelson, Mr. Pearson, Mr. Randolph, Mr. Ribicoff, Mr. Schmitt, Mr. Schweiker, Mr. Sparkman, Mr. Stevens, Mr. Thurmond, Mr. Tower, Mr. Wallop, Mr. Young, and Mr. Zorinsky

This bill allows a refundable tax credit for tuition paid to institutions of higher education (including institutions for graduate study), vocational schools, and accredited and tax-exempt secondary or elementary schools by a taxpayer for himself, for his spouse, or for any dependents for whom the taxpayer is entitled to claim a personal exemption under section 151(e). The credit is 50 percent of the tuition expenses paid by a taxpayer during a taxable year, but is limited to a maximum of $500 with respect to the tuition paid for any individual. If more than one taxpayer pays an individual's tuition, the credit must be prorated among such taxpayers. A credit is allowed for a spouse's expenses only if the taxpayer is entitled to an exemption for his spouse under section 151(b) or they file a joint return. No trade or business expense deduction under section 162 may be claimed for any tuition taken into account in determining this credit.

The bill applies to taxable years beginning after December 31, 1979.

B. AMENDMENT TO SOCIAL SECURITY FINANCING AMENDMENTS OF 1977

The Social Security Financing Amendments of 1977, as passed by the Senate, contained an amendment sponsored by Senator Roth to provide a tax credit for certain educational expenses. This amendment was deleted from the bill by the conferees.

The amendment (as modified by Senator Bumpers' amendment) allowed a refundable tax credit for education expenses paid by an individual, for himself, his spouse, or his dependents. The credit covered 100 percent of the eligible educational expenses at institutions of higher education or vocational schools up to a maximum of $250 for any one individual.

21-296—78——2

If more than one taxpayer paid the educational expenses of an individual, the credit with respect to that individual had to be prorated among such taxpayers.

Educational expenses of a taxpayer's spouse could be claimed only if the taxpayer was entitled to an exemption for his spouse under section 151(b) or if they filed a joint return. The credit was allowed only with respect to fulltime students. Expenses taken into account in determining a credit had to be reduced by scholarship or fellowship grants excluded from income under section 117 and educational assistance allowances and educational and training allowances received under chapters 35 and 33 (relating to Veterans' benefits), respectively, of title 38 of the United States Code. Eligible expenses were tuition, fees, books, supplies, and equipment, but did not include meals, lodging, or similar personal, living, or family expenses. Higher education expenses had to be for courses allowed as credit toward a baccalaureate degree. Vocational school expenses had to be for courses allowed as credit for a certificate of required course work. No trade or business expense deduction under section 162 was allowed for expenses taken into account in determining the credit.

The amendment applied to educational expenses paid after December 31, 1977, in taxable years beginning after December 31, 1977.

III. BACKGROUND

A PRESENT LAW

Present law provides no tax credit, deduction, nor other tax benefit for personal educational expenses. However, educational expenses which qualify as trade or business expenses under section 162 may be deducted. (In some circumstances, tuition and related expenses have qualified as medical expenses, deductible under sec. 213.) In addition, individuals generally may exclude from income amounts received as scholarships and fellowships (sec. 117). Generally, a taxpayer may claim a $750 personal exemption deduction (and a $35 credit) for each dependent but only if that dependent has less than $750 gross income for the taxable year. However, the gross income limitation does not apply if the dependent is the taxpayer's child and either (1) the child is younger than 19 or (2) the child is a student (sec. 151). Also, charitable contributions to exempt educational institutions are deductible for income tax purposes on a preferred basis (sec. 170). The scholarship exclusion, personal exemption for students, and deductibility of gifts to schools, under present law, are expected to produce fiscal 1978 tax expenditures of $285 million, $770 million, and $805 million, respectively.

d. Types of Students

B. PRIOR CONGRESSIONAL ACTION

In the 1950's, tax deductions against adjusted gross income for some portion of college expenses and an additional personal exemption for each student were the most common legislative proposals for tax relief for education expenses. In the 1960's, tax credit proposals became popular. From 1967 to 1977, six education tax credit proposals passed the Senate, but none was ever approved by the House of Representatives.

Senator Ribicoff was the chief sponsor of the first Senate-approved education tax credit measure. His 1967 amendment would have provided taxpayers a nonrefundable credit for college expenses equal to 75 percent of the first $200 of expenses, 25 percent of the next $300, and 10 percent of expenses between $500 and $1,500. This credit was reduced by one percent of the taxpayer's adjusted gross income above $25,000.

In 1969, the Senate again passed a tax credit amendment sponsored by Senator Ribicoff. This measure was generally similar to the 1967 amendment except that high-income taxpayers would have benefited somewhat less.

In 1971, the Senate passed its third education tax credit. The measure, introduced by Senator Hollings, was identical to the 1967 Ribicoff proposal except that the Hollings credit was refundable.

The Hollings amendment was dropped in conference on H.R. 10947, the Revenue Act of 1971.

In 1976, Senator Roth sponsored an amendment to provide a non-refundable tax credit of up to $250 per student when fully phased in. Unlike the Ribicoff and Hollings amendments, the Roth credit was 100 percent of expenses (although the credit could not exceed tuition expenses) and was not phased out for high-income taxpayers. The Roth amendment was added to H.R. 10612, the Tax Reform Act of 1976, but the conference committee deleted it. Subsequently, the Senate passed the Roth proposal as an amendment to a tariff bill, H.R. 1386. A unanimous consent request for a conference on the bill was objected to in the House, and the legislation died at the end of the 94th Congress.

In 1977, the Senate approved a $250 education tax credit offered by Senator Roth as an amendment to H.R. 9346, the Social Security Financing Amendments of 1977. A floor amendment made the credit refundable during its first year so that direct payments would be made to those whose tax liability was less than the credit. This amendment was dropped in the House-Senate conference.

1. Constitutionality

The constitutionality of providing Federal tax benefits to nonpublic school students or their parents has long been a subject of debate. No case dealing with tax credits or deductions directly related to the actual cost of non-public school tuition has been decided by the Supreme Court. However, in *Committee for Public Education and Religious Liberty* v. *Nyquist*, 413 U.S. 756 (1973), the Court held that a New York State income tax deduction for each child attending a nonpublic secondary or elementary school in an amount unrelated to the actual cost of tuition violated the establishment clause of the First Amendment of the U.S. Constitution.[1] Although the *Nyquist* decision did not specifically deal with tax credits or deductions, based on the actual cost of tuition, the Court's opinion suggests that these types of benefits also might be unconstitutional. In testing the constitutionality of a statute under the establishment clause of the First Amendment, the Court applied three cumulative tests:[2]

(1) the statute must have a secular purpose;

(2) the primary effect of the statute must neither advance nor inhibit religion; and

(3) the statute must not foster excessive government entanglement with religion.

The Court found that the New York State statute met the secular purpose test, but held that the statute failed the primary effect test, and indicated *in dicta* that prospects for passing the excessive entanglement test were not good.

Although tax credits or deductions for nonpublic elementary or secondary schools may entail constitutional difficulties, Federal aid to church-related colleges and universities has generally been regarded more favorably by the Supreme Court. In upholding construction

---

[1] The First Amendment states that: "Congress shall make no law respecting an establishment of religion or prohibiting the free exercise thereof; * * *"

[2] To be found constitutional under the establishment clause, a statute must pass all three tests. *Lemon* v. *Kurtzman*, 403 U.S. 602 (1971).

grants to church-related colleges and universities for nonsectarian facilities, the Court found in *Tilton* v. *Richardson*, 403 U.S. 672 (1971) that there was much less likelihood that religion would permeate secular education at that level, and thus the risk that government aid would support religious activities or foster excessive government entanglement with religion was significantly reduced.

C. ISSUES

2. Goals of Education Tax Benefits

Educational tax benefits can be directed at various education and tax policies. These include providing financial aid to middle-income and upper middle-income families; maintaining the financial viability of higher education institutions; improving tax equity; and perfecting the definition of taxable income.

a. Providing Financial Aid to Middle-Income Families

Cost of post secondary education

College expenses have increased dramatically over the last ten years. The overall cost of a private college education rose 118.8 percent between 1964 and 1976. Fees at public universities have also risen substantially—98.4 percent during the same time period. (See Table 1, below.)

TABLE 1.—PERCENTAGE OF TOTAL COLLEGE COSTS PAID FROM VARIOUS SOURCES, BY INCOME LEVEL

Source	Parental income level: Low (<$8,000)	Middle ($8,000 to 19,999)	High ($20,000 or more)	Al students
BEOG	27.0	7.3	1.5	8.3
SEOG	3.2	1.1	.2	1.1
State scholarship	5.9	4.7	1.4	3.7
Local, private scholarship	4.0	4.5	2.6	3.8
Student's GI benefits	1.9	1.0	.4	.9
Parents' GI benefits	1.0	.6	.3	.5
SS dependents' benefits	5.4	1.8	.7	1.9
Total grants	48.4	21.0	7.1	20.2
Parents or family	18.6	36.8	62.9	43.1
Spouse	.7	.4	.3	.4
Total family assistance	19.3	37.2	63.2	43.5
Total grants and family assistance	67.7	58.2	70.3	63.7
College work study	4.3	2.3	.6	2.0
Federal guaranteed student loan	2.6	3.6	1.8	2.8
National direct student loan	3.0	2.6	.7	2.0
Other loan	1.3	2.0	1.3	1.6
Full-time work	2.0	2.5	1.8	2.2
Part-time work	10.0	15.5	12.2	13.5
Savings	7.0	11.2	9.4	9.9
Other financing	2.0	1.9	1.8	1.9
Student net cost	32.2	41.6	29.6	35.9
Grand total	99.9	99.8	99.9	99.6

Nete: Totals do not equal 100 percent due to rounding.

Scurce: Unpublished analyses conducted by the Higher Education Research Institute based on data from the national survey of freshmen entering college in 1975 as reported in Astin, A. W.; King, M. R.; and Richardson, G. T. "The American Freshman," Los Angeles: Laboratory for Research in Higher Education, University of Californ a, Los Angeles, 1975.

According to the College Entrance Examination Board, the average annual cost of attending a public university has increased 40 percent in the past 5 years, from $1,782 to $2,790. For a private university, the cost has increased 35 percent from $2,793 to $4,568. According to a New York Times survey, the total annual costs at many colleges and universities are as high as $7,000. Supporting one child through undergraduate school can cost $10,000 to $25,000.

Tuition costs will continue to increase. It has been estimated that it will cost $47,000 to attend a public university and $82,000 for a private university in the 1990's.

While the costs of education have increased greatly, the median family income also has risen at a rate comparable to the rate of increase in student charges at institutions of higher education for the years 1967–1976.

Between 1969 and 1974, the U.S. Census Bureau reports that the percentage of 18 to 24 year olds attending college full time decreased 22 percent while enrollment for lower and higher income students remained fairly stable. Increasing costs are the primary reason. In addition, Census Bureau data shows that many families have more than one child of college age at the same time. Middle- and lower-income families who do not qualify for financial aid but who cannot keep up with the increases in college expenses have voiced particular concern about the increased cost of higher education.

Nonpublic education

Many low- and middle-income parents whose children attend nonpublic schools bear a very heavy financial burden. The cost of nonpublic elementary and secondary education has increased substantially in recent years, and it is expected that this increase will continue. At the same time, the cost of public schools also is rising substantially, and taxes keep increasing to meet these cost increases. As a result, nonpublic school parents must pay for the increased costs of both public and nonpublic schools, even though they relieve the public schools of the cost of educating their children. This financial burden is an important factor in accounting for the declining enrollment and the closing of many nonpublic schools.

Nonpublic schools represent an integral part of our society providing diversity of choice and healthy competition for public education. Many Americans express themselves socially, ethnically and culturally through nonpublic educational institutions. These institutions often provide stability to urban neighborhoods by motivating parents to stay in the cities. Finally, nonpublic schools relieve the public school system, and thus all taxpayers supporting public schools, of very substantial costs. The closing of many nonpublic schools would increase taxes significantly.[3]

b. Maintaining the Financial Viability of Higher Education Institutions

While almost all educational institutions have financial problems, the plight of private or independent institutions is particularly grave.

[3] The President's Commission on School Finance estimated that public school operating costs would increase from $1.3 billion to $3.2 billion, and capital costs from $4.7 to $10 billion. President's Commission on School Finance, "Schools, People, and Money," p. 55 (1972).

Some proponents of education tax benefits have argued that such benefits (or other forms of government subsidy) are needed to preserve the United States' plural system of education. Some fear that, without new subsidies, independent educational institutions will no longer be financially viable.

c. Perfecting the Definition of Taxable Income

Some tax theoreticians believe education tax benefits would improve the calculation of taxable income. The tax law now allows businesses to deduct certain expenses incurred in the production of income, for example, depreciation on capital investments. The expenses of obtaining a college education might be viewed as costs associated with the production of future income—an investment in human capital. If one adopts this view, then the current definition of taxable income should be changed to allow deductions for college expenses as a form of capital investment.

d. Improving Tax Equity

Fairness among taxpayers is a major tax policy goal. The ability-to-pay principle of taxation underlying the tax law means that taxpayers who are similarly situated should pay the same taxes (horizonal equity) while those with different taxpaying capacity should pay different amounts of taxes (vertical equity). The tax law recognizes that income alone is not an adequate measure of taxpaying capacity. Various exemptions, exclusions, deductions, and credits have been incorporated as refinements of that measure.

Most advocates of education tax benefits have implicity claimed that such benefits would improve tax equity. For example, it is often stated that families with more than one child attending college at the same time need tax relief because they are especially burdened. Implicitly, such statements suggest that the taxpaying capacity of these families is reduced. Education tax benefits would lower the taxes of taxpayers incurring education expenses compared to the taxes paid by taxpayers without such expenses.

3. Forms of Education Tax Benefits

The design of a tax benefit is important for achieving different policy goals. There are three basic forms for such benefits: (1) a deduction against adjusted gross (or gross) income; (2) a credit against tax liability; and (3) a deferral (or postponement) of tax payments.

Deductions

Tax deductions for education expenses would reduce taxable income. The usual base for deductions is adjusted gross income. However, a deduction from gross income would extend the benefits to all taxpayers, even those who do not itemize.[4] he value of a deduction

[4] Adjusted gross income is the income base from which the taxpayer subtracts excess itemized deductions (that is, itemized deductions in excess of the zero bracket amount) to arrive at taxable income. Adjusted gross income is basically an individual's gross income minus moving and certain other expenses incurred by employees in earning that income, payments by the self-employed and employees to retirement plans, alimony, and the 50 percent capital gains deduction. If a tax deduction for education expenses were made to apply to adjusted gross income, it would be an itemized deduction which could not be claimed by taxpayers whose itemized deductions are less than the zero bracket amount. However,

varies directly with the marginal tax rate of the taxpayer and is worth more to high-income taxpayers than to those with low incomes. For example, a $100 deduction s worth $70 to someone with a 70 percent top marginal tax rate but only $30 to a taxpayer with a 30 percent marginal tax rate.

Credits

In contrast to a tax deduction which reduces the tax base, a tax credit reduces the taxpayer's tax liability directly, and has the same absolute dollar value for all taxpayers. For example, a $100 tax credit has an after-tax value of $100 (unless the taxpayer does not have $100 of tax liablility to be offset by the credit),[5] while a $100 tax deduction has an after-tax value ranging from $14 to $70. Measured in terms of after-tax income, a tax credit provides the same benefit to those in high- and low-income brackets whereas a deduction provides a larger benefit to those in higher income brackets.

Deferral

Tax deferrals for education expenses can be viewed as a form of loan which grants relief by postponing tax payments. The repayment of deferred taxes can be spread over several years. To provide greater relief while the student is attending school, repayment may begin after the student leaves school. Interest charges reduce the cost to the Treasury. However, a low interest rate or interest-free loan provides a greater subsidy.

4. Eligible expenses

a. Types of Costs

Proponents of education tax benefits generally have restricted eligible expenses to those closely associated with instruction. Personal expenses such as room, board, and travel generally have not been covered.

Under these proposals, tax benefits generally would be disallowed for expenses which are not borne by the student or his family. For example, tax credits and deduction generally would be reduced by scholarships, tax-exempt veterans' benefits, and amounts paid by employers.

b. Limitations

The amount of expenses to be covered by a tax benefit must be considered. Tax credits can be set at a constant or changing rate. For example, a credit could offset 50 percent of all qualified expenses or it could cover a changing proportion of expenses if set at 100 percent of the first $1,000 for expenses, 50 percent of the next $1,000, and 5 percent of the third $1,000. Tax benefits which provide little or no benefit for some base or minimum level of expenditures channel the assistance to students attending relatively more expensive institutions. Benefits set at low, flat dollar amounts help costly institutions less.

---

if it were treated in the same way as moving expenses—a subtraction from gross income made in arriving at adjusted gross income—all taxpayers, even nonitemizers, would benefit from it.

[5] If a tax credit is made "refundable," those whose tax liability is less than the credit would receive a cash payment equal to the difference.

A benefit ceiling or maximum may be set. Benefits with high ceilings would cover a greater share of expenses and be important for higher-cost schools. However, unless other restrictions are imposed, high ceilings also will reduce the relative cost of attending low-cost institutions and might worsen the competitive position of higher-cost institutions.

c. Eligible Institutions

In providing a tax benefit, it must be decided whether the benefit should be extended to all levels of education or whether some levels of education should be excluded. Qualifications for eligible institutions also may be established. Most bills have required that the eligible institutions be accredited and qualify as tax-exempt organizations. (This latter restriction, in effect, requires that the school, in order to be eligible, have a racially nondiscriminatory policy.) In order to prevent abuse, many bills have required that the school, in order to be eligible, offer education on a regular basis; many bills have denied benefits for noncredit and recreational courses.

d. Types of Students

Many bills have restricted tax benefits to full-time students. However, if aid to educational institutions, tax equity, or definition of taxable income are considered, extending benefits to part-time students might be appropriate.

O